April 10, 2009

VIA ELECTRONIC FILING

Mr. Charles L.A. Terreni
Chief Clerk of the Commission
S.C. Public Service Commission
P.O. Drawer 11649
Columbia, SC 29211

RE: Application of Carolina Power and Light Company d/b/a Progress Energy Carolinas, Incorporated for the Establishment of Procedures for DSM/EE Programs (Docket No. 2008-251-E)

Dear Mr. Terreni:

Please find attached for electronic filing in the above-referenced docket the Brief of Environmental Defense Fund, South Carolina Coastal Conservation League, Southern Alliance for Clean Energy and the Southern Environmental Law Center. By copy of this letter I am serving a copy of the same on all parties of record via electronic mail and U.S. Mail. If you have questions, please do not hesitate to contact me.

Sincerely,

s/Sarah Rispin

Enclosure
Cc (w/encl.): Parties of Record (via electronic mail)

BEFORE THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA

DOCKET NO. 2008-251-E

In re:	)	
Application of Carolina Power and	)	JOINT BRIEF OF
Light Company d/b/a Progress	)	ENVIRONMENTAL
Energy Carolinas, Incorporated for	)	INTERVENORS
the Establishment of Procedures for	)	
DSM/EE Programs	)	

PURSUANT to S.C. Reg. 103-851 and the South Carolina Public Service Commission ("the Commission") Chairman Fleming's oral order of February 12, 2009, intervenors Southern Alliance for Clean Energy, Environmental Defense Fund, South Carolina Coastal Conservation League and the Southern Environmental Law Center (collectively, "Environmental Intervenors"), by and through the undersigned counsel, submit the following brief on the Establishment of Procedures for Demand-Side Management and Energy Efficiency Programs proposed by Carolina Power and Light ("Progress" or "the Company").

I. INTRODUCTION

While Environmental Intervenors support the basic concept that an electrical utility should receive a financial incentive sufficient to encourage pursuit of all cost-effective energy efficiency, Progress Energy has not filed sufficient information with this Commission to support its present request for such incentives. The filing contains no information on the energy efficiency programs Progress seeks to implement. Nor does the filing contain any support for the unusually generous incentive structure the Company seeks. Without this information, the Commission cannot evaluate whether the required rate increases would be worthwhile. We urge the Commission to reject Progress's request at this time, and order the Company to re-file an application that includes an

energy efficiency target, a set of programs for achieving that target, and an incentive structure accompanied by supporting documentation showing that they are necessary to incentivize the Company to implement demand-side management and energy efficiency programs. Only then would the Commission be able to evaluate Progress's request to ensure that the accompanying rate increases would achieve the fundamental economic goal of any energy efficiency program—to bring down long-term costs by creating extra capacity in the system and obviating the need for new generation facilities.

II. STATEMENT OF THE CASE

On June 27, 2008, Progress filed its application for approval of its "Application for the Establishment of Procedures for DSM/EE Programs" by the Commission. In its application, filed pursuant to S.C. Code Ann. § 58-37-20, Progress said that the procedures it sought would "encourage [Progress] investment in cost effective energy efficient technologies and energy conservation programs and . . . allow recovery of all costs associated with such programs and . . . an appropriate incentive for investing in such programs." The filing did not specify any DSM or EE programs that Progress planned to implement as a result of the incentives it sought. For those unspecified programs, Progress sought to be allowed to (a) capitalize the costs, (b) recover all associated net lost revenues, and (c) an incentive equal to 50% of the net present value of any associated shared savings. The filing did include an industrial opt-out provision, allowing "[a]ny industrial customer or large commercial customer that notifies PEC that it has implemented or, in accordance with stated, quantifiable goals, will implement

alternative demand-side management or energy efficiency programs" to opt out of PEC's programs, and be exempt from the associated rate increases.

On January 8, 2009, Progress filed a revised cost recovery and incentive mechanism, along with direct testimony in support of its application. At that time, Progress included a brief outline of how it might evaluate potential DSM/EE measures, requiring them to be commercially available, "sufficiently mature," "applicable to the PEC service area[,] demographics[,] and climate," feasible, and cost-effective. The proposal did not, however, provide any details of any of the programs PEC sought to implement. The cost recovery mechanism had changed somewhat: Progress sought to be allowed to (a) capitalize the costs of the programs over a period of ten years, at the overall weighted average net-of-tax rate of return approved in its most recent general rate case, (b) 36 months of net lost revenues, and (c) an incentive equal to 8% of the shared savings associated with DSM programs, and 13% of the shared savings associated with its EE programs. This new cost-recovery mechanism matched that for which it was seeking approval in North Carolina before that state's utility commission; to the extent the numbers changed, they were apparently based on a negotiated settlement with the North Carolina Public Staff in that proceeding. Tr. Vol. 1 at 64, lines 23-25 (Testimony of B. Mitchell Williams). Finally, according to the accompanying direct testimony, the opt-out provision from the June 27, 2008 filing remained in place.

On January 14, 2009, Progress filed a third DSM/EE Cost Recovery Procedure and Mechanism, to clarify that the June 27, 2008 filing had been superseded by the January 8, 2009 filing. And on January 23, 2009, Progress filed a fourth DSM/EE Cost Recovery Procedure and Mechanism, as part of a settlement reached with the South

Carolina Office of Regulatory Staff and intervenors Wal-Mart Stores East, LP, and Nucor Steel-South Carolina. Although the cover letter accompanying the January 23 filing stated that it was "entirely consistent with the testimony filed by [Progress] on January 8, 2009 and the DSM/EE procedure for cost recovery filed by [Progress] on January 14, 2009," in fact, the industrial and large-customer opt-out provision had been changed substantially: As of that final filing, the application stated only that "[c]ommercial customers with annual consumption of 1,000,000 kWh or greater in the billing months of the prior calendar year and all industrial customers *may elect not to participate in PEC's demand-side management and energy efficiency programs by notifying PEC of the customer's election in writing.*" (emphasis added). This removed the requirement that the large commercial and industrial customers implement their own alternative demand-side management or energy efficiency programs to qualify to opt out.

Environmental Intervenors filed direct testimony on January 22, 2009 and surrebuttal testimony on February 5, 2009, offering a critique of Progress's application and suggestions as to how it could be improved.

On February 11, 2009 the Commission held a formal evidentiary hearing, at which the Company and Environmental Intervenors presented witnesses.

III. LEGAL FRAMEWORK

The General Assembly has vested the Commission with "power and jurisdiction to supervise and regulate the rates and service of every public utility in this State . . . ." S.C. Code Ann. § 58-3-140 (2007). An electric utility must file with the Commission "schedules showing all rates . . . established by the electrical utility and collected or

enforced or to be collected or enforced within the jurisdiction of the commission." S.C. Code Ann. § 58-27-820 (2007).

In setting rates, the Commission is bound by the principle that "[e]very rate made, demanded or received by any electrical utility . . . shall be just and reasonable." S.C. Code Ann. § 58-27-810 (2007). See In re Application of South Carolina Electric & Gas Company for Adjustments in the Company's Electric Rate Schedules and Tariffs, Docket No. 2004-178-E, Order No. 2005-2 (S.C. P.S.C., Jan. 6, 2005) ("[i]n setting rates, the Commission must determine a fair rate of return that the utility should be allowed the opportunity to earn after recovery of the expenses of utility operations."). This process "involves the balancing of the investor and the consumer interests." Southern Bell Telephone and Telegraph Co. v. South Carolina Public Service Commission, 270 S.C. 590, 595, 244 S.E. 2d. 278, 281 (1978). Specifically:

> A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public *equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises* or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties.

Id. at 596, 244 S.E. 2d. at 281 (quoting Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679, 692-73 (1923)) (emphasis added).

Where changes in rates or tariffs are proposed, the Commission must "hold a public hearing concerning the lawfulness or reasonableness" of the proposed changes, and must document fully its determination of "a fair rate of return based exclusively on

reliable, probative, and substantial evidence on the whole record." S.C. Code Ann. § 58-27-870. While "[n]othing in the plain language of the statute requires the PSC to adopt any one particular . . . methodology" in setting rates, Nucor Steel v. S.C. Pub. Service Commission, 312 S.C. 79, 85, 439 S.E.2d 270, 273 (1994) (construing identical language in S.C. Code Ann. § 58-5-240(H)), the Commission has employed the following guidelines in evaluating rates of return requested by electric utilities:

> 1) The rate of return should be sufficient to allow [the utility] the opportunity to earn a return equal to firms facing similar risks;
> 2) The rate of return should be adequate to assure investors of the financial soundness of the utility and to support the utility's credit and ability to raise capital needed for on-going utility operations at reasonable cost;
> 3) The rate of return should be determined with due regard for the present business and capital market conditions facing the utility;
> 4) The rate of return is not formula-based, but requires an informed expert judgment by the Commission balancing the interests of shareholders and customers.

In re Application of South Carolina Electric & Gas Company for Adjustments in the Company's Electric Rate Schedules and Tariffs, Docket No. 2004-178-E, Order No. 2005-2 (S.C. P.S.C. Jan. 6, 2005). See also In re Application of South Carolina Electric & Gas Company for an Increase in its Electric Rates and Charges, Docket No. 2002-223-E, Order No. 2003-38, 225 P.U.R.4th 440 (S.C. P.S.C., Jan. 31, 2003) (same).

Progress's request in this proceeding for a new compensation mechanism and a rider on rates also implicates S.C. Code Ann. § 58-37-20, which governs the adoption of procedures encouraging energy efficiency and conservation. That section provides, in relevant part, that

> the Commission may adopt procedures that encourage electrical utilities . . . to invest in cost-effective energy efficient technologies and energy conservation programs. If adopted, these procedures must: provide incentives and cost recovery for energy suppliers and distributors who invest in energy supply and end-use technologies that are cost-effective,

> environmentally acceptable, and reduce energy consumption or demand; allow energy suppliers and distributors to recover costs and obtain a reasonable rate of return on their investment in qualified demand-side management programs sufficient to make these programs at least as financially attractive as construction of new generating facilities; require the Public Service Commission to establish rates and charges that ensure that the net income of an electrical or gas utility regulated by the commission after implementation of specific cost-effective energy conservation measures is at least as high as the net income would have been if the energy conservation measures had not been implemented.

S.C. Code Ann. § 58-37-20.

IV. ARGUMENT

Under the proposed compensation mechanism, Progress seeks three layers of compensation for its as-yet unspecified demand-side management and energy efficiency programs:

1. Cost recovery *plus* the cost of capitalizing all costs that, in its discretion, it decides to capitalize[1] over a *ten year period* at the overall weighted average net-of-tax rate of return approved in its most recent general rate case;
2. Net lost revenues over a thirty-six month period; and
3. A "program performance incentive" (PPI) of 8-13%.

In other words, Progress will receive (1) the incentive it receives for investing in conventional power plants, *see* Tr. Vol. I at 68-69 (Testimony of B. Mitchell Williams); (2) net lost revenues to make it whole for encouraging efficiency; *and* (3) a program performance incentive on top of that. And all of this without regard for whether it achieves a certain level of energy efficiency savings, because it has established no target

[1] When asked about how Progress determined what expenses would be capitalized, Mr. Williams, speaking for Progress, could answer only that "There will likely be some costs that would not be expensed; they would be capitalized . . . and we would earn a return on the unamortized balance." Tr. Vol. I at 80 (Testimony of B. Mitchell Williams).

for its energy efficiency programs—nor, indeed, any such programs. This produces two immediate and obvious flaws, which are discussed in detail below.

A. Progress's Compensation Scheme is Overly Rich and Out of Keeping with Commission Precedent.

Under South Carolina law, Progress must show that this compensation is "just and reasonable," S.C. Code Ann. § 58-27-810, and would result in a "fair rate of return" to the Company, S.C. Code Ann. § 58-27-870. Progress must also show that this compensation is in line with "that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties." Southern Bell Telephone and Telegraph Co., 270 S.C. at 595.

Progress has offered scant support for the appropriateness of this structure. It did not point to, and indeed cannot point to, any other electric utility in the region or in the country which has been allowed to earn returns on whatever portion of its DSM/EE costs it decides to amortize, *and* net lost revenues *and* a performance incentive on top of that. While Ms. Bateman did offer oral evidence that shared savings granted to utilities in other states ranged from 10-25 percent, Tr. Vol. I at 160 (Testimony of Laura Bateman), she offered no evidence that such utilities were also allowed to recover net lost revenues and capitalized returns. *Id.* at 161 (stating that "I'm not aware of what [utilities in those states] are allowed" to recover in addition to their performance incentives); *id.* at 163 ("I think this particular combination is – I'm not aware of any other state that does it.").

PEC, in asking for this three-part recovery mechanism, is asking for an incredibly generous package. While it is common for one or two of these parts to comprise a compensation package for DSM and/or EE, PEC could not, on cross-examination,

identify a precedent under which any other utility received such a rich compensation package. By asking for all three, PEC is seeking an incentive out of proportion to the risk and actual financing costs associated with DSM/EE programs. Such an excessive level of compensation cannot be considered appropriate.

B. Without Any Indication of Targets or Programs, No Compensation Can Be Justifies

Notably absent from the Progress's application in this docket was any indication whatsoever of the programs it plans to implement. It is, in essence, saying to this Commission that it should grant them the above-described incentives and rates of return for whatever energy efficiency and demand side management programs it happens to do. In other words, Progress is asking the Commission to approve rate increases to pay for its energy efficiency and demand side management programs whether or not they produce sufficient savings in terms of the amount of electricity that Progress must generate to justify the capital, start-up, and management costs of such programs. Under the current proposal, Progress would receive all of the incentives whether it achieves 10 MW in savings, or 3000.

PEC has defended the lack of any target or goal by saying that it could not set one until it received the results of a market potential study that it commissioned at some point in 2007 or 2008. Tr. Vol. I at 165 (Testimony of Laura Bateman). But the Company still has little knowledge about when that study is can be expected to be completed. *Id.* at 164. And nonetheless, the absence of the results from a market potential study is not a reason to reject targets. PEC can look to other sources to establish interim targets, and bring forward its market potential study in the future as a basis for revising those targets.

Without a tie to performance targets, Environmental Intervenors submit, granting a "performance target" is not appropriate.

As for its lack of any program outlines, Progress avers that they are simply not relevant, because all that is at issue in this proceeding is the incentive structure. But this defies basic logic. One cannot decide the rate one is going to pay for someone's services without knowing anything about the services they offer; nor can this Commission make an informed decision about the incentives it will offer Progress to implement demand-side management and energy efficiency programs without knowing anything about those programs. If, for instance, Progress is going to roll out about 10 MW in energy-efficiency savings, the Commission might be justified in deciding that it is not worth the ratepayers' money to richly compensate Progress for that amount of savings, as it will not obviate the need for any new generation. If, on the other hand, Progress was designing programs that, with a fair amount of hard work, could generate savings equivalent to the annual output of a 800 MW power plant, the Commission would be justified in deciding that it *should* richly compensate Progress for that amount of savings, as long as the overall cost to ratepayers remained lower than the cost of building and running such a plant. But the Commission has no way of knowing what Progress has in mind. Approving a rich incentive structure before even the barest contours of such programs are revealed is virtually *per se* unreasonable.

C. Conclusion

Progress has presented this Commission with a flawed and incomplete filing, in which it is asking for up-front approval of a cost-recovery mechanism for amounts of

energy efficiency/demand-side management savings it refuses to specify, through programs it likewise refuses to elucidate. Accordingly, the Environmental Intervenors respectfully request that the Commission grant the following relief:

1. Disapprove the Company's proposed EE/DSM compensation structure.

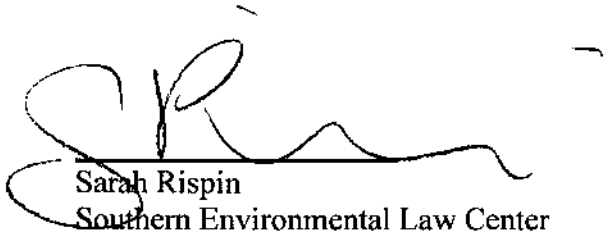
2. Request that the Company refile its proposed EE/DSM compensation structure accompanied by:

    a. A target for EE and DSM savings that it plans to achieve through such programs.

    b. A menu of programs through which it will achieve those programs

    c. A compensation structure for those programs based on documented incentives structures granted to other utilities that have a demonstrated ability to incentivize substantial EE and DSM savings.

Respectfully submitted, this 10th day of April, 2009.



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CERTIFICATE OF SERVICE

I hereby certify that the following persons have been served with the Pre-Filed Direct Testimony of Rick Hornby and Brian Henderson on behalf of Southern Alliance for Clean Energy, the Natural Resources Defense Council, the South Carolina Coastal Conservation League, and the Southern Environmental Law Center.

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This 10th day of April, 2009

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